

**REPORT OF THE AUDIT OF THE
LEE COUNTY
FISCAL COURT**

**For The Fiscal Year Ended
June 30, 2003**



**CRIT LUALLEN
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EXECUTIVE SUMMARY

AUDIT EXAMINATION OF THE LEE COUNTY FISCAL COURT

**For The Fiscal Year Ended
June 30, 2003**

The Auditor of Public Accounts has completed the Lee County Fiscal Court audit for fiscal year ended June 30, 2003. We have issued an unqualified opinion on the financial statements taken as a whole. Based upon the audit work performed, the financial statements are presented fairly in all material respects.

Financial Condition:

Fund balances decreased by \$526,385 from the beginning of the year, resulting in a cash surplus of \$367,084 as of June 30, 2003. The decrease in fund balances was due to FEMA expenditures not being reimbursed by the end of the fiscal year.

Debt Obligations:

Capital lease principal agreements totaled \$373,753 as of June 30, 2003. Future principal and interest payments of \$444,634 are needed to meet these obligations.

Report Comment:

- The County Should Improve Their Internal Control Procedures

Deposits:

The fiscal court's deposits were insured and collateralized by bank securities or bonds.

CONTENTS

PAGE

INDEPENDENT AUDITOR’S REPORT	1
LEE COUNTY OFFICIALS	3
STATEMENT OF ASSETS, LIABILITIES, AND EQUITY ARISING FROM CASH TRANSACTIONS	7
STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND CHANGES IN CASH BALANCES	10
NOTES TO FINANCIAL STATEMENTS	12
SUPPORTING SCHEDULES:	
COMPARATIVE SCHEDULE OF BUDGETED TO ACTUAL OPERATING REVENUE	21
SCHEDULE OF OPERATING REVENUE	25
COMPARATIVE SCHEDULE OF FINAL BUDGET AND BUDGETED EXPENDITURES	29
REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	33
REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133.....	37
SCHEDULE OF FINDINGS AND QUESTIONED COSTS	41
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS	45
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS	46
APPENDIX A:	
CERTIFICATION OF COMPLIANCE - LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM	



CRIT LUALLEN
Auditor of Public Accounts

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Robbie Rudolph, Secretary
Finance and Administration Cabinet
Honorable L. C. Reese, Lee County Judge/Executive
Members of the Lee County Fiscal Court

Independent Auditor's Report

We have audited the accompanying statement of assets, liabilities, and equity arising from cash transactions of Lee County, Kentucky, as of June 30, 2003, and the statement of cash receipts, cash disbursements, and changes in cash balances for the year then ended. These financial statements are the responsibility of the Lee County Fiscal Court. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Fiscal Court Audits issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, Lee County, Kentucky, prepares its financial statements on a prescribed basis of accounting that demonstrates compliance with the modified cash basis and laws of Kentucky, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets, liabilities, and equity arising primarily from cash transactions of Lee County, Kentucky, as of June 30, 2003, and the revenues received and expenditures paid for the year then ended, in conformity with the modified cash basis of accounting.



To the People of Kentucky
Honorable Ernie Fletcher, Governor
Robbie Rudolph, Secretary
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Members of the Lee County Fiscal Court

In accordance with Government Auditing Standards, we have also issued our report dated November 13, 2003, on our consideration of Lee County, Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The accompanying financial information listed as supporting schedules in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements of Lee County, Kentucky. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Based on the results of our audit, we present the schedule of findings and questioned costs, included herein, which discusses the following report comment:

- The County Should Improve Their Internal Control Procedures

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a stylized, flowing script.

Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
November 13, 2003

LEE COUNTY OFFICIALS

For The Fiscal Year Ended June 30, 2003

Fiscal Court Members:

L. C. Reese	County Judge/Executive
Ronnie P. Begley	Magistrate
Everett L. Marshall	Magistrate
Benny Todd	Magistrate
Carl Ross	Magistrate

Other Elected Officials:

Tom Jones	County Attorney
Arthur Noe	Jailer
Russell Stamper	County Clerk
Emma Adams	Circuit Court Clerk
Harvey Pelfrey	Sheriff
Gary Lutes	Property Valuation Administrator
Emmett Daugherty	Coroner

Appointed Personnel:

Pearl Spencer	County Treasurer
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STATEMENT OF ASSETS, LIABILITIES,
AND EQUITY ARISING FROM CASH TRANSACTIONS

LEE COUNTY
STATEMENT OF ASSETS, LIABILITIES,
AND EQUITY ARISING FROM CASH TRANSACTIONS

June 30, 2003

Governmental
Fund Types

General

Assets and Other Resources

Assets

Cash and Cash Equivalents	\$ 367,084
Accounts Receivable (Note 4)	<u>82,764</u>
Total Assets	<u>\$ 449,848</u>

Other Resources

Amounts to Be Provided
in Future Years for:

Capital Leases (Note 5 A-F)	<u>\$ 373,753</u>
Total Other Resources	<u>\$ 373,753</u>
Total Assets and Other Resources	<u><u>\$ 823,601</u></u>

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
 STATEMENT OF ASSETS, LIABILITIES,
 AND EQUITY ARISING FROM CASH TRANSACTIONS
 June 30, 2003
 (Continued)

	<u>Governmental Fund Types</u>
	<u>General</u>
<u>Liabilities and Equity</u>	
<u>Liabilities</u>	
Capital Lease (Note 5 A-F)	<u>\$ 373,753</u>
Total Liabilities	<u>\$ 373,753</u>
<u>Fund Balances</u>	
Fund Balances:	
Unreserved	<u>\$ 449,848</u>
Total Equity	<u>\$ 449,848</u>
Total Liabilities and Fund Balances	<u><u>\$ 823,601</u></u>

The accompanying notes are an integral part of the financial statements.

STATEMENT OF CASH RECEIPTS,
CASH DISBURSEMENTS, AND CHANGES IN CASH BALANCES

LEE COUNTY
STATEMENT OF CASH RECEIPTS,
CASH DISBURSEMENTS, AND CHANGES IN CASH BALANCES

For The Fiscal Year Ended June 30, 2003

	General Fund Type			
	General Fund	Road and Bridge Fund	Jail Fund	Local Government Economic Assistance Fund
<u>Cash Receipts</u>				
Schedule of Operating Revenue	\$ 853,771	\$ 1,351,175	\$ 37,516	\$ 219,761
Other Financing Sources:				
Transfers In	169,000	300,000	147,765	
Kentucky Advance Revenue Program	297,000	42,500		
Total Cash Receipts	<u>\$ 1,319,771</u>	<u>\$ 1,693,675</u>	<u>\$ 185,281</u>	<u>\$ 219,761</u>
<u>Cash Disbursements</u>				
Comparative Schedule of Final Budget and Budgeted Expenditures	\$ 903,424	\$ 1,503,497	\$ 188,319	\$ 377,403
Other Financing Uses:				
Transfers Out	351,000	125,000		147,765
Capital Leases:				
Principal Paid	9,370	49,208		
Kentucky Advance Revenue Program Repaid	297,000	42,500		
Total Cash Disbursements	<u>\$ 1,560,794</u>	<u>\$ 1,720,205</u>	<u>\$ 188,319</u>	<u>\$ 525,168</u>
Excess (Deficiency) of Cash Receipts Over (Under) Cash Disbursements	\$ (241,023)	\$ (26,530)	\$ (3,038)	\$ (305,407)
Cash Balance - July 1, 2002*	<u>472,519</u>	<u>48,251</u>	<u>10,394</u>	<u>325,475</u>
Cash Balance - June 30, 2003*	<u><u>\$ 231,496</u></u>	<u><u>\$ 21,721</u></u>	<u><u>\$ 7,356</u></u>	<u><u>\$ 20,068</u></u>

* Cash Balance Includes Investments

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
 STATEMENT OF CASH RECEIPTS,
 CASH DISBURSEMENTS, AND CHANGES IN CASH BALANCES
 For The Fiscal Year Ended June 30, 2003
 (Continued)

<u>General Fund Type</u>		
<u>Ambulance Fund</u>	<u>Solid Waste Fund</u>	<u>Totals (Memorandum Only)</u>
\$ 798,132	\$ 34,932	\$ 3,295,287
44,000	7,000	667,765
		339,500
<u>\$ 842,132</u>	<u>\$ 41,932</u>	<u>\$ 4,302,552</u>
\$ 744,618	\$ 29,210	\$ 3,746,471
44,000		667,765
16,623		75,201
		339,500
<u>\$ 805,241</u>	<u>\$ 29,210</u>	<u>\$ 4,828,937</u>
\$ 36,891	\$ 12,722	\$ (526,385)
35,670	1,160	893,469
<u>\$ 72,561</u>	<u>\$ 13,882</u>	<u>\$ 367,084</u>

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS

June 30, 2003

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

The financial statements of Lee County include the funds, agencies, boards, and entities for which the fiscal court is financially accountable. Financial accountability, as defined by Section 2100 of the GASB Codification of Governmental Accounting and Financial Reporting Standards, as amended by GASB 14, was determined on the basis of the government's ability to significantly influence operations, select the governing authority, participate in fiscal management and the scope of public service. Based upon the application of the criteria stated in GASB 14, management should include the Public Service Corporation as part of the reporting entity.

Public Service Corporation

The Public Service Corporation is a legally separate entity established to provide debt service for the purchase of real estate property from the Kentucky Mountains Farm Cooperative. The Public Service Corporation's governing body consists entirely of Fiscal Court members. Therefore, management should include the Public Service Corporation as a component unit, and its financial activity should be blended with the Fiscal Court. However, the Public Service Corporation had no financial activity during the year and had no financial information to blend with that of the fiscal court.

Additional - Lee County Constitutional Elected Officials

- Circuit Court Clerk
- County Attorney
- County Clerk
- County Sheriff
- Property Valuation Administrator

The Kentucky constitution provides for election of the above officials from the geographic area constituting Lee County. Pursuant to state statute, these officials perform various services for the Commonwealth of Kentucky, its judicial courts, the fiscal court, various cities and special districts within the county, and the board of education. In exercising these responsibilities, however, they are required to comply with state laws. Audits of their financial statements are issued separately and individually and can be obtained from their respective administrative offices.

B. Fund Accounting

Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. The government uses funds to report on its financial position and the results of its operations. A fund is a separate accounting entity with a self-balancing set of accounts. Lee County Fiscal Court's fund types, a definition of each, and county funds included within each fund type are listed below.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

B. Fund Accounting (Continued)

1) General Fund Type

General Fund Type accounts for all financial resources except those required to be accounted for in another fund type. The Lee County General Fund Type includes the following county funds: General Fund, Road and Bridge Fund, Jail Fund, Local Government Economic Assistance Fund, Ambulance Fund, and the Solid Waste Fund.

2) Debt Service Fund Type

Debt Service Fund Type accounts for the accumulation of resources for the payment of general long-term debt principal and interest and includes funds for the Public Service Corporation. Debt service is provided through annual transfers from the General Fund Type in the amount of the debt service requirements for the year. However, the Public Service Corporation had no financial activity for the year.

C. Basis of Accounting

For all fund types, the county utilizes a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this basis of accounting, assets, liabilities, and related revenues and expenditures are recorded when they result from cash transactions, with a few exceptions. This modified cash basis recognizes revenues when received, and expenditures are recognized when paid. Long-term receivables, long-term obligations and amounts to be provided in future years to retire debt are recorded in the financial statements. The amount to be provided in future years to retire debt is offset by any cash or cash equivalents held by the county in a bond or debt service fund.

The State Local Finance Officer does not require the county to maintain a general fixed assets group of accounts; therefore the value of the county's fixed assets is not included in the financial statements. These fixed assets include buildings, equipment and land that are owned by the county.

D. Legal Compliance - Budget

The Lee County budget is adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer. The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

D. Legal Compliance - Budget (Continued)

Formal budgets are not adopted for the Public Service Corporation Fund (Debt Service Fund) because lease contractual provisions require specific payments to and from this fund annually and transfers are budgeted in the General Fund Type to comply with these requirements. The Department for Local Government does not require this fund to be budgeted. Furthermore, there was no activity for the year.

E. Cash and Investments

Cash includes amounts in bank accounts, and investments are stated at cost. Investments may include certificates of deposit on the financial statements; however, for the purpose of disclosing credit risk (Note 3), investments exclude certificates of deposit.

KRS 66.480 authorizes the county to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

F. Joint Ventures

A legal entity or other organization that results from a contractual agreement and that is owned, operated, or governed by two or more participants as a separate activity subject to joint control, in which the participants retain (a) an ongoing financial interest or (b) an ongoing financial responsibility is a joint venture.

The Lee County Fiscal Court has entered into a joint venture with Wolfe and Owsley counties. They have formed the Three Forks Public Properties Corporation, a legally separate organization, in order to sell bonds to build the Three Forks Regional Jail. The Lee County Fiscal Court does not appoint a voting majority of the 10 board members; however, Lee County does appoint 4 members whereas, Wolfe and Owsley counties each appoint 3 members. The Three Forks Public Properties Corporation issued \$6,295,000 of First Mortgage Revenue Bonds for the construction of the regional jail. Each county will be equally liable if the Three Forks Regional Jail doesn't meet the bond payment requirements. Each of the three participants will have joint control in which they have an ongoing financial interest and ongoing financial responsibility. Each county has also guaranteed the Three Forks Regional Jail payment for 15 prisoners at a rate of \$25 a day each even if occupancy is at a lower amount.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 2. Employee Retirement System

The county has elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a multiple-employer public retirement system which covers all eligible full-time employees. Benefit contributions and provisions are established by statute. Nonhazardous covered employees are required to contribute 5 percent of their salary to the plan. The county's contribution rate for nonhazardous employees was 6.34 percent.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report.

Note 3. Deposits

The county maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the county and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. These requirements were met, and as of June 30, 2003, the county's deposits were fully insured or collateralized at a 100% level with collateral of either pledged securities held by the county's agent in the county's name, or provided surety bond which named the county as beneficiary/obligee on the bond.

Note 4. Receivable

The county has \$82,764 of accounts receivable in the Ambulance Fund. These accounts receivable are comprised of customer billings.

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 5. Capital Leases

- A. In June 1995, the county entered into a capital lease agreement for \$99,000 with Kentucky Association of Counties Leasing Trust Program for a grader. Terms of the agreement stipulate a ten-year repayment schedule, with variable monthly interest payments and variable annual principal payments. The principal amount is due on January 20 of each year to end on January 20, 2005. As of June 30, 2003, the principal was \$24,000. Lease payments for the remaining years are:

<u>Fiscal Year Ended June 30</u>	<u>Scheduled Interest</u>	<u>Scheduled Principal</u>
2004	\$ 1,140	\$ 12,000
2005	420	12,000
Totals	<u>\$ 1,560</u>	<u>\$ 24,000</u>

- B. In July 1997, the county entered into a capital lease agreement for \$71,000 with Kentucky Association of Counties Leasing Trust Program for a truck and a backhoe. Terms of the agreement stipulate a ten-year repayment schedule, with variable monthly interest payments and variable annual principal payments. The principal amount is due on January 20 of each year to end on January 20, 2007. As of June 30, 2003, the principal was \$24,000. Lease payments for the remaining years are:

<u>Fiscal Year Ended June 30</u>	<u>Scheduled Interest</u>	<u>Scheduled Principal</u>
2004	\$ 1,207	\$ 6,000
2005	868	6,000
2006	532	6,000
2007	196	6,000
Totals	<u>\$ 2,803</u>	<u>\$ 24,000</u>

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 5. Capital Leases (Continued)

- C. In September 1999, the county entered into a capital lease agreement for \$43,945 with Kentucky Association of Counties Leasing Trust Program for voting machines. Terms of the agreement stipulate a five-year repayment schedule, with variable monthly interest payments and variable monthly principal payments. As of June 30, 2003, the principal was \$11,822. Lease payments for the remaining years are:

<u>Fiscal Year Ended</u> <u>June 30</u>	<u>Scheduled</u> <u>Interest</u>	<u>Scheduled</u> <u>Principal</u>
2004	\$ 223	\$ 9,424
2005	12	2,398
Totals	<u>\$ 235</u>	<u>\$ 11,822</u>

- D. In July 2000, the county entered into a capital lease agreement for \$48,510 with Kentucky Association of Counties Leasing Trust Program for a brush cutter. Terms of the agreement stipulate a five-year repayment schedule, with variable monthly interest payments and variable monthly principal payments. As of June 30, 2003, the principal was \$21,609. Lease payments for the remaining years are:

<u>Fiscal Year Ended</u> <u>June 30</u>	<u>Scheduled</u> <u>Interest</u>	<u>Scheduled</u> <u>Principal</u>
2004	\$ 502	\$ 10,213
2005	193	10,506
2006	2	890
Totals	<u>\$ 697</u>	<u>\$ 21,609</u>

- E. In June 2001, the county entered into a capital lease agreement for \$49,955 with Kentucky Association of Counties Leasing Trust Program for an ambulance. Terms of the agreement stipulate a three-year repayment schedule, with variable monthly interest payments and variable monthly principal payments. As of June 30, 2003, the principal was \$17,322. Lease payments for the remaining years are:

<u>Fiscal Year Ended</u> <u>June 30</u>	<u>Scheduled</u> <u>Interest</u>	<u>Scheduled</u> <u>Principal</u>
2004	\$ 287	\$ 17,322
Totals	<u>\$ 287</u>	<u>\$ 17,322</u>

LEE COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 5. Capital Leases (Continued)

- F. In May 2002, the county entered into a capital lease agreement for \$300,000 with Kentucky Association of Counties Leasing Trust Program for road paving. Terms of the agreement stipulate a ten-year repayment schedule, with variable monthly interest payments and variable annual principal payments. The principal amount is due on January 20 of each year to end on January 20, 2012. As of June 30, 2003, the principal was \$275,000. Lease payments for the remaining years are:

Fiscal Year Ended June 30	Scheduled Interest	Scheduled Principal
2004	\$ 12,889	\$ 25,000
2005	11,671	25,000
2006	10,352	30,000
2007	8,890	30,000
2008	7,429	30,000
2009-2012	14,068	135,000
Totals	<u>\$ 65,299</u>	<u>\$ 275,000</u>

Note 6. Insurance

For the fiscal year ended June 30, 2003, Lee County was a member of the Kentucky Association of Counties' All Lines Fund (KALF). KALF is a self-insurance fund and was organized to obtain lower cost coverage for general liability, property damage, public officials' errors and omissions, public liability, and other damages. The basic nature of a self-insurance program is that of a collectively shared risk by its members. If losses incurred for covered claims exceed the resources contributed by the members, the members are responsible for payment of the excess losses.

COMPARATIVE SCHEDULE OF
BUDGETED TO ACTUAL OPERATING REVENUE

LEE COUNTY
COMPARATIVE SCHEDULE OF
BUDGETED TO ACTUAL OPERATING REVENUE

For The Fiscal Year Ended June 30, 2003

<u>Budgeted Funds</u>	Budgeted Operating Revenue	Actual Operating Revenue	Over (Under) Budget
<u>General Fund Type</u>			
General Fund	\$ 938,156	\$ 853,771	\$ (84,385)
Road and Bridge Fund	1,576,704	1,351,175	(225,529)
Jail Fund	188,636	37,516	(151,120)
Local Government Economic Assistance Fund	178,735	219,761	41,026
Ambulance Fund	750,306	798,132	47,826
Solid Waste Fund	30,884	34,932	4,048
Totals	<u>\$ 3,663,421</u>	<u>\$ 3,295,287</u>	<u>\$ (368,134)</u>

Reconciliation

Total Budgeted Operating Revenue Above	\$ 3,663,421
Add: Budgeted Prior Year Surplus	674,575
Less: Other Financing Uses	<u>(342,895)</u>
Total Operating Budget Per Comparative Schedule Of Final Budget and Budgeted Expenditures	<u>\$ 3,995,101</u>

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SCHEDULE OF OPERATING REVENUE

LEE COUNTY
SCHEDULE OF OPERATING REVENUE

For The Fiscal Year Ended June 30, 2003

	GOVERNMENTAL FUND TYPE
<u>Revenue Categories</u>	<u>General Fund Type</u>
Taxes	\$ 612,567
In Lieu Tax Payments	16,604
Excess Fees	802
Licenses and Permits	31,291
Intergovernmental Revenues	1,794,274
Charges for Services	688,011
Miscellaneous Revenues	135,088
Interest Earned	16,650
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Total Operating Revenue	\$ 3,295,287
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COMPARATIVE SCHEDULE OF
FINAL BUDGET AND BUDGETED EXPENDITURES

LEE COUNTY
COMPARATIVE SCHEDULE OF
FINAL BUDGET AND BUDGETED EXPENDITURES

For The Fiscal Year Ended June 30, 2003

Expenditure Categories	GENERAL FUND TYPE		
	Final Budget	Budgeted Expenditures	Under (Over) Budget
General Government	\$ 428,529	\$ 442,122	\$ (13,593)
Protection to Persons and Property	820,990	917,244	(96,254)
General Health and Sanitation	42,340	117,162	(74,822)
Social Services	17,425	24,568	(7,143)
Recreation and Culture	200,700	5,501	195,199
Roads	1,354,667	1,492,430	(137,763)
Debt Service	109,118	22,829	86,289
Capital Projects	500,007	388,807	111,200
Administration	521,325	335,808	185,517
Total Operating Budget - General Fund Type	\$ 3,995,101	\$ 3,746,471	\$ 248,630
Other Financing Uses:			
Borrowed Money-			
Kentucky Advanced Revenue Program - Principal	299,970	339,500	(39,530)
Capital Lease Agreements - Principal	42,925	75,201	(32,276)
TOTAL BUDGET - GENERAL FUND TYPE	<u>\$ 4,337,996</u>	<u>\$ 4,161,172</u>	<u>\$ 176,824</u>

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REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



CRIT LUALLEN
Auditor of Public Accounts

To the People of Kentucky
Honorable Ernie Fletcher, Governor
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Members of the Lee County Fiscal Court

**Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards**

We have audited the financial statements of Lee County, Kentucky, as of and for the year ended June 30, 2003, and have issued our report thereon dated November 13, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Lee County's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Lee County's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition.

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PHONE 502.573.0050 FACSIMILE 502.573.0067

AN EQUAL OPPORTUNITY EMPLOYER M/F/D



Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards
(Continued)

Internal Control Over Financial Reporting (Continued)

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect Lee County's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the accompanying schedule of findings and questioned costs.

- The County Should Improve Their Internal Control Procedures

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe that the reportable condition described above is a material weakness.

This report is intended solely for the information and use of management, federal awarding agencies, and pass-through entities, and is not intended to be, and should not be, used by anyone other than the specified parties.

Respectfully submitted,



Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
November 13, 2003

REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL
CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133



CRIT LUALLEN
Auditor of Public Accounts

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Robbie Rudolph, Secretary
Finance and Administration Cabinet
Honorable L. C. Reese, Lee County Judge/Executive
Members of the Lee County Fiscal Court

**Report On Compliance With Requirements
Applicable To Each Major Program And On Internal Control
Over Compliance In Accordance With OMB Circular A-133**

Compliance

We have audited the compliance of Lee County, Kentucky, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2003. Lee County's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Lee County's management. Our responsibility is to express an opinion on Lee County's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Lee County's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Lee County's compliance with those requirements.

In our opinion, Lee County complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2003.



Report On Compliance With Requirements
Applicable To Each Major Program And On Internal Control
Over Compliance In Accordance With OMB Circular A-133
(Continued)

Internal Control Over Compliance

The management of Lee County is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Lee County's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management, federal awarding agencies, and pass-through entities, and is not intended to be, and should not be, used by anyone other than the specified parties.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
November 13, 2003

FINDINGS AND QUESTIONED COSTS

LEE COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For The Fiscal Year Ended June 30, 2003

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of Lee County.
2. One reportable condition disclosed during the audit of the financial statements is reported in the Independent Auditor's Report. The condition reported is not a material weakness.
3. No instances of noncompliance material to the financial statements of Lee County were disclosed during the audit.
4. No reportable conditions relating to the audit of the major federal awards programs are reported in the Independent Auditor's Report.
5. The auditor's report on compliance for the audit of the major federal awards programs for Lee County expresses an unqualified opinion.
6. There are no audit findings relative to the major federal awards programs for Lee County reported in Part C of this schedule.
7. The program tested as a major program was: FEMA-DR-1407 (CFDA #83.544)
8. The threshold for distinguishing Type A and B programs was \$300,000.
9. Lee County was not determined to be a low-risk auditee.

B. FINDINGS - FINANCIAL STATEMENTS AUDIT

REPORTABLE CONDITION:

2003-01 The County Should Improve Their Internal Control Procedures

The Department for Local Government requires the Judge/Executive to keep certain records and make certain reports. These duties include:

- receiving all claims, and preparing a master claim list to present to the fiscal court
- preparing all checks
- maintaining an appropriation ledger
- being responsible for the county's quarterly report
- reconciling appropriation ledger to the treasurer's appropriation ledger
- issuing purchase orders and maintaining a purchase order log
- maintaining time records (vacation/sick).

The Treasurer is currently completing these procedures. Someone other than the Treasurer should implement the above duties. This would help strengthen controls.

The County has a lack of adequate segregation of duties. Due to the entity's diversity of official operations, small size and budget restrictions the county has limited options for establishing an adequate segregation of duties. We recommend the following compensating controls be implemented to offset this internal control weakness:

- An independent person should list all receipts and agree them back to the treasurer's receipt ledger.
- An independent person should compare fiscal court order approvals to invoices and cancelled checks.

County Judge Executive's Response:

Will try to segregate more duties, an independent person does do bank reconciliations.

LEE COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For The Fiscal Year Ended June 30, 2003
(Continued)

NONCOMPLIANCES:

None.

PRIOR YEAR FINDINGS FINANCIAL STATEMENT AUDIT

The County Should Improve Their Internal Control Procedures

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARDS PROGRAM
AUDIT

None.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

LEE COUNTY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For The Fiscal Year Ended June 30, 2003

Federal Grantor Program Title <u>Grant Name (CFDA #)</u>	<u>Pass-Through Grantor's Number</u>	<u>Expenditures</u>
Cash Programs:		
<u>U.S. Department of Agriculture</u>		
Action Team (CFDA #10.766)	Not Available	\$ 5,000
Ambulance (CFDA #10.766)	Not Available	28,000
<u>U.S. Department of Commerce</u>		
Economic Development Administration		
Lee County Industrial Park (CFDA #11.307)	Not Applicable	95,737
<u>U. S. Federal Emergency Management Agency</u>		
Passed-Through State Department of Military Affairs:		
Disaster and Emergency Assistance Grants-		
2003 Flooding (CFDA #83.544)	FEMA-DR-1407	<u>473,056</u>
Total Cash Expenditures of Federal Awards		<u>\$ 601,793</u>

LEE COUNTY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For The Fiscal Year Ended June 30, 2003

Note 1 - Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Lee County, Kentucky and is presented on a modified cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

CERTIFICATION OF COMPLIANCE -
LOCAL GOVERNMENT ECONOMIC ASSISTANCE

LEE COUNTY FISCAL COURT

For The Fiscal Year Ended
June 30, 2003

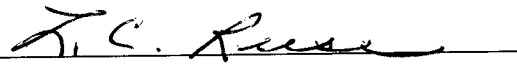
CERTIFICATION OF COMPLIANCE

LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM

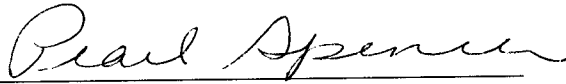
LEE COUNTY FISCAL COURT

Fiscal Year Ended June 30, 2003

The Lee County Fiscal Court hereby certifies that assistance received from the Local Government Economic Assistance Program was expended for the purpose intended as dictated by the applicable Kentucky Revised Statutes.



L.C. Reese
County Judge/Executive



Pearl Spencer
County Treasurer

